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October 18, 1999

BY HAND DELIVERY

Ms. Magalie R. Salas
Secretary
Federal Communications Commission
445 Twelfth Street, SW
Washington, D.C. 20554

Re: Qwest Communications International Inc. and U S WEST, Inc. Applications for Transfer of Control CC Docket No. 99-272

Dear Ms. Salas:

Pursuant to the FCC's Public Notice FCC 99-1775, released September 1, 1999, enclosed for filing in the above-referenced docket are the original and four copies of the Response to Comments on Applications for Transfer of Control of Qwest Communications International Inc. ("Qwest") and U S WEST, Inc. ("U S WEST"). Also, we have forwarded a diskette containing the response to CeCi Stephens of the Policy and Program Planning Division of the Common Carrier Bureau.

Please contact the undersigned with any questions concerning Qwest. In the event of any questions concerning U S WEST, please contact Daniel L. Poole at (303) 672-2794.

Respectfully submitted,

Peter A. Rohrbach
Counsel for Qwest Communications International Inc.

Enclosures

cc: Office of Public Affairs
Margaret Egler, Common Carrier Bureau
Lauren Kravetz, Wireless Telecommunications Bureau
Joanna Lowry, International Bureau
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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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OFFICE OF THE SECRETARY

In the Matter of	)	
	)	CC Docket No. 99-272
Merger of Qwest Communications	)	
International Inc. and	)	File No. 18-EX-TC-1999
U S WEST, Inc.	)	et. al.

RESPONSE TO COMMENTS ON APPLICATIONS FOR TRANSFER OF CONTROL

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Dated: October 18, 1999

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To: The Commission

RESPONSE TO COMMENTS ON APPLICATIONS FOR TRANSFER OF CONTROL

Qwest Communications International Inc. ("Qwest") and U S WEST, Inc. ("U S WEST"), by their attorneys, submit this joint response to the comments and petitions to deny filed in connection with the above-captioned request for consent to the transfer of control of Commission authorizations (the "Application").

SUMMARY

The record in this proceeding clearly demonstrates that the merger of Qwest and U S WEST is in the public interest and should be approved without delay. Comments here fall into two basic categories. First, some parties argue that the Commission should deny the merger unless it first imposes a wide range of conditions, many of them drawn in cookie-cutter fashion from the large ILEC-ILEC transactions. However, these parties cannot establish any legal predicate for such conditions. They barely try to demonstrate any public interest harm arising from the Qwest-U S WEST merger itself. They ignore the fact that this vertical merger

is completely different from other combinations involving horizontal expansion of ILEC market position.

Commenters also attempt to sweep the merger's important public interest benefits under the rug. They ignore the applicants' showing that the merger will, among other benefits, promote the deployment of advanced services both within and outside the US WEST region. Commenters do not address the fact that the merger will permit the applicants to compete better with the much larger telecom companies created by mergers that already have occurred (or are in prospect).

In particular, commenters disregard the important new incentives the merger will create for the combined company to satisfy Section 271 as soon as possible. Pending 271 relief, Qwest will face significant competitive disadvantages in the national interexchange market due to the hole in its service territory created by divestiture. Meanwhile, the combined company already will own a state of the art network asset it could use for in-region interLATA service, and the opportunity cost of leaving that wasting asset idle will be large. Together these business problems will significantly increase incentives for the combined company to re-enter the interLATA market in the U S WEST region.

At bottom, these commenters have simply cataloged their individual complaints regarding U S WEST. But these grievances are not caused by the merger, and are not relevant here. The merger clearly meets the public interest standards of the Communications Act. Commenters should pursue their issues in the other proceedings and forums that are available to them.

The second category of comments relate to Qwest's commitment to divest its in-region interLATA services prior to closing. Some parties assert that the Commission should delay action on this Application pending further scrutiny of Qwest's steps to carry out this divestiture. These arguments are nothing but unsupported allegations that Qwest will violate Section 271 by providing prohibited services after the merger closing. However, the parties have no foundation for this suggestion whatsoever. Qwest further demonstrates its commitment to comply with the Act by providing a description of its divestiture plan here. But the task for the Commission is only to review and rule on the merger application. The Commission should not accept commenters' suggestion that it also micro-manage the steps Qwest takes to divest before closing.

That said, divestiture provides an important reason for prompt Commission approval of this Application. Qwest has much to do to prepare for divestiture, including negotiations with potential buyers of the services to be discontinued, operational work to make the transition trouble-free for customers, and coordination with customers themselves. In order for that process to run smoothly, Qwest and the buyers will need as much lead time as possible. However, Qwest anticipates that potential buyers may be reluctant to expend the significant resources required by this project while formal Commission approval remains pending.

Given the lack of substantive issues presented by this merger, the Commission can readily serve the interests of customers by approving the Application as promptly as possible. The sooner it does so, the more smoothly the divestiture process will run for all concerned. 1/

I. THE MERGER IS IN THE PUBLIC INTEREST AND SHOULD BE APPROVED WITHOUT CONDITIONS.

A. The Standard of Review.

This merger easily satisfies the public interest standards of Sections 214(a) and 310(d) of the Act. Qwest and U S WEST demonstrated in their Application that the merger will be pro-consumer and pro-competition. The merger will bring together two firms with complementary assets and skill sets, and better position them to implement their shared goal: to become a leading provider of broadband-based services as the Internet revolutionizes communications in this country and around the world.

A handful of commenters nevertheless oppose the merger unless the Commission attaches conditions to its approval. These commenters (referred to here as the "Merger Opponents") consist entirely of parties with preexisting disagreements with U S WEST over issues related to the company's local exchange

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1/ As the Commission knows, the Department of Justice and the FTC already have given early termination to their review of this transaction in the Hart-Scott-Rodino process. Although state approval processes also are pending, divestiture activity will be less affected by them. Section 271 is a federal issue, and once the Commission has approved this merger the work to implement divestiture can proceed in full.

telephone activities. These parties urge the Commission to hold this application hostage and address their individual grievances through merger conditions.

The Merger Opponents, however, ignore the relevant legal standard. The Commission is not free to attach conditions to a merger in order to enhance the array of pro-competitive benefits offered by the transaction; instead, any condition attached must address a specific anti-competitive risk or harm created by the merger itself. 2/ Congress invested the Commission with only limited authority to attach conditions to its approval of merger transactions. 3/ In recent merger cases, the Commission has consistently acknowledged its limited authority to impose

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2/ In the AT&T-TCI and MCI-WorldCom merger proceedings, the Commission repeatedly declined invitations to impose conditions not directly related to anti-competitive effects of those transactions. In the AT&T-TCI proceeding, for example, the Commission declined to impose a condition granting competitors a right of access to the merged company's multichannel video programming facilities in light of its conclusion that the merger would be "unlikely to result in the loss of a significant source of current or future competition in MVPD services." *Application for Transfer of Control of Tele-Communications, Inc. to AT&T*, ("*AT&T-TCI Order*"), 14 FCC Rcd 3160, 3173 ¶ 22 (1999). Likewise, because the Commission concluded that the MCI-WorldCom merger was "not likely to have anticompetitive effects on the provision of * * * private line service on any U.S. international route," it refused to condition its approval on a divestiture of any such facilities. *Application for Transfer of Control of MCI Communications to WorldCom, Inc.* ("*MCI-WorldCom Order*"), 13 FCC Rcd 18025, 18101, ¶ 135 (1998).

3/ Section 214(c) of the Communications Act permits the Commission to attach to a certificate only "such terms and conditions as * * * the public convenience and necessity may require." 47 U.S.C. § 214(c). Likewise, section 303(r) of the Act restricts the Commission to "prescrib[ing] such restrictions and conditions * * * *as may be necessary* to carry out the provisions of the chapter." 47 U.S.C. § 303(r) (emphasis added).

conditions only "where necessary * * * to ensure that the public interest is served by [a] transaction." 4/

In this case the Merger Opponents utterly fail to establish the predicate for conditions. They fail to show how the merger would in any respect harm the public interest. And they entirely discount -- or simply ignore -- the important consumer benefits that will flow from the merger.

Before turning to the allegations made by the Merger Opponents, both Qwest and U S WEST wish to recognize and affirm U S WEST's continuing obligations, and the obligations of the merged company, as an incumbent local exchange carrier under both state and federal law. The applicants are committed to meeting those obligations and continuing to provide high quality, reliable service to the millions of existing U S WEST residential and business local exchange subscribers. The applicants firmly believe the merger will benefit the mass of customers who depend on telephone service for basic communications. The merger will create a stronger entity better able to meet those needs, as well as future telecommunications requirements.

B. OPPONENTS CANNOT SQUEEZE THIS VERTICAL MERGER INTO THE "ILEC-ILEC" BOX.

Merger Opponents predictably take their cue from the Commission's recent consideration of other transactions where conditions were imposed, most

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4/ *See e.g.*, *AT&T-TCI Order*, 14 FCC Rcd at 3169, ¶ 15; *MCI-WorldCom Order*, 13 FCC Rcd at 18032, ¶ 10.

notably the Bell Atlantic-NYNEX and SBC-Ameritech combinations. 5/ However, the Qwest-U S WEST merger is fundamentally different from the horizontal ILEC-ILEC deals the Commission has recently confronted. This transaction is a vertical combination of (i) an ILEC and (ii) a nondominant interexchange carrier with the large majority of its operations outside the ILEC's region. This vertical merger creates none of the risks to local or long distance competition that may be presented when two major ILECs come together.

More specifically, the Commission and parties opposing the recent ILEC-ILEC mergers have identified three principal anticompetitive risks potentially created by those combinations. First, ILEC-ILEC mergers may retard the development of new competition by eliminating a "significant" potential independent competitor with extensive experience in the local exchange market. In the Bell Atlantic-NYNEX proceeding, for example, the Commission noted that the merger would "eliminate any prospect of NYNEX competing with Bell Atlantic in the * * * northeast corridor." 6/ Second, by increasing the size of one company's "footprint" of access lines, ILEC-ILEC mergers may enhance the ability and incentive of the merged entity to discriminate against CLECs. 7/ Finally, the

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5/ *See, e.g.,* Covad Comments at ii (comparing this proceeding to those involving the "SBC-PacTel, SBC-SNET, SBC-Ameritech, Bell Atlantic-NYNEX, and Bell Atlantic-GTE mergers" without any analysis of similarities or differences between those mergers and the merger at issue here).

6/ *Applications for Consent to Transfer Control of NYNEX to Bell Atlantic* ("*Bell Atlantic-NYNEX Order*"), 12 FCC Rcd 19985, 19991, ¶ 9 (1997).

7/ *Id.* at ¶ 103.

merger of two ILECs may impair the Commission's ability to monitor or "benchmark" ILEC performance. 8/

None of those competitive concerns arise in connection with this transaction. These matters are discussed in more detail in the attached declaration of Dennis Carlton and Hal Sider of Lexecon, Inc. ("Carlton/Sider Declaration"), provided here as Attachment A. As they explain, Qwest is not an ILEC, and its CLEC business in U S WEST's region is trivial. Qwest has purchased conduit in a fiber ring facility under construction in Seattle that traverses both U S WEST and GTE territory. 9/ Qwest otherwise is not a facilities-based local service provider in any market in the U S WEST region. Furthermore, Qwest had already decided to cease its local resale operations in the U S WEST region well before entering into the proposed merger. The process of exiting the local resale market is now substantially complete. 10/ Covad's assertion that the merger will result in heightened barriers to entry in high speed access markets is also unfounded. 11/ Qwest has begun to offer DSL service in U S WEST's region, but it does so only as a reseller of the DSL services of Rhythms and of Covad itself. 12/

8/ *Id.* at ¶ 151.

9/ In any event, other facilities-based CLECs are active in Seattle. *See* Carlton/Sider Declaration, Attachment A, at 15.

10/ The only exception relates to minimal local resale associated with service to payphones.

11/ Covad Communications Comments at 9-10.

12/ The merger clearly will not block the development of any long distance competition. U S WEST, of course, has no in-region interexchange business, and its

McLeod points to Qwest's partial interest in Advanced Radio Telecom (ART), a nationwide 39 GHz wireless service provider, as additional evidence of in-region Qwest CLEC activity. 13/ However, Qwest's 19 percent, non-controlling interest in ART does not make Qwest a provider of competitive wireless services, and thus does not bear on Qwest's status as an actual or potential competitor to U S WEST. But even if ART were wholly-owned by Qwest, no competitive or other public interest issue would arise. The Commission already has determined that ILECs such as U S WEST should be allowed to hold licenses for 39 GHz spectrum within their service areas. 14/ If U S WEST would be eligible to own these licenses outright, there should be even less concern with the merged company having a less than controlling interest in any such licensee.

Likewise, the proposed transaction raises no risk of increased incentive to discriminate against CLECs. This matter is discussed in more detail in the

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out-of-region business constitutes a minuscule percentage of any competitive market.

13/ McLeod Comments at 16. McLeod also points to Qwest's ownership interest in Covad as evidence of its in-region CLEC activity. McLeod Comments at 17. However, Qwest's tiny ownership interests in Covad and Rhythms (less than three percent in each case) are too small to create any competitive issues.

14/ The Commission determined that the restrictions it had imposed on ILEC use of frequencies in a different band -- the LMDS band -- were not necessary in the 37-40 GHz band because of the differences in the nature of the spectrum and because of the wide range of potential and actual competitors to licensees in the band. *Amendment of the Commission's Rules Regarding the 37.0-38. GHz and 38.6-40.0 GHz Bands, Report and Order and Second Notice of Proposed Rulemaking*, FCC 97-391, released Nov. 3, 1997, 12 FCC Rcd 18600, 18617-18628 (1997), *aff'd on recon., Amendment of the Commission's Rules Regarding the 37.0-38.6 GHz and 38.6-40.0 GHz Bands*, ET Docket No. 95-183 (released July 29, 1999) ("*39 GHz Order*").

Carlton/Sider Declaration. The simple fact is that Qwest is not an ILEC and the merger will not increase the number of access lines controlled by the merged entity. Because the transaction does not increase the "footprint" of U S WEST's access lines, it will not augment the merged entity's ability or incentive to discriminate against CLECs. 15/ Nor will the Qwest-U S WEST combination eliminate any opportunities for monitoring ILEC performance; every "benchmark" available to federal and state regulators today will remain after the merger. Accordingly, the Commission should dismiss any suggestion by commenters that conditions deemed appropriate for the recent ILEC-ILEC mergers should apply here.

Allegiance Telecom, Inc. ("Allegiance") tries to make a backdoor argument along the same vein, asserting that ILEC-ILEC merger conditions are justified by BellSouth's 9.9% equity stake in Qwest. 16/ Congress has already determined that equity interests of 10% or less do not raise questions of common ownership, control, or affiliation. 17/ In any event, Allegiance is confused regarding the facts. BellSouth's interest in the combined company will be less than 5% due to dilution of its interest from the merger. BellSouth is entitled to a single Board seat once it has satisfied certain Section 271 requirements itself. None of this gives BellSouth a control position in the combined company or otherwise converts the

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15/ Quite the contrary, powerful new incentives for the merged entity to obtain Section 271 authority, as discussed below, can only result in increased opportunities for competitive entry into these markets. *See* Section I.C.3, *infra*; Declaration of Bruce M. Owen, Economists Inc. ("Owen Declaration"), provided as Attachment B.

16/ Allegiance Comments at 3-5, 10-13.

17/ *See* 47 U.S.C. § 153(1).

Qwest-U S WEST merger into an ILEC-ILEC combination. 18/ BellSouth's *de minimis* equity stake in Qwest is of no relevance to this transaction; the merged entity and BellSouth each will retain full autonomy to pursue their respective corporate interests. 19/

In short, opponents' attempts to squeeze this application into the "ILEC-ILEC" box disregard the facts. This vertical merger is entirely different from those horizontal combinations. No public interest problems arise here to complicate the Commission's analysis under Sections 214 and 310.

C. OPPONENTS IGNORE THE MERGER'S AFFIRMATIVE PUBLIC INTEREST BENEFITS.

In addition to alleging harms where none exist, Merger Opponents also disregard the merger benefits identified in the Application. 20/ However, these pro-

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18/ Allegiance erroneously states that BellSouth has an "option" to acquire up to 20% of the combined company. *See* Allegiance Comments at 2. This is incorrect. BellSouth does not have any right to purchase shares from Qwest, nor does Qwest have any obligation to sell BellSouth additional shares. Allegiance may be confused about a former standstill provision that limited BellSouth's ability to acquire more than 20% of Qwest without Qwest board approval. That provision is no longer in effect.

19/ Indeed, throughout the Hart-Scott-Rodino process for the Qwest-U S WEST merger, the Department of Justice was well aware of BellSouth's equity stake in Qwest. It did not object or request any changes to the merger. While Qwest and BellSouth will retain their existing marketing agreement, both parties are fully aware that any coordinated marketing must comply with the restrictions outlined in recent Commission orders. *See, e.g., AT&T Corp. v. Ameritech Corp.*, 13 FCC Rcd 21438 (1998), *aff'd, U S WEST v. FCC*, 177 F.3d 224 (D.C.Cir. 1999) *("Teaming Order"); Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended,* Third Order on Reconsideration, CC Docket No. 96-149, FCC 99-242, ¶39 (rel. Oct. 1, 1999).

20/ *See, e.g.*, Covad Comments at 22-23 (asserting that the merger has no benefits).

consumer and pro-competition benefits are far too large and important to be swept under the rug. This merger is founded on a conclusion by both Qwest and U S WEST that they must combine in order to better serve the public as technology -- and other larger mergers -- revolutionize the telecommunications landscape. Indeed, Qwest believes so strongly in this principle that it is willing to take the difficult step of divesting its in-region interLATA services now to position itself to achieve these benefits in the future.

Qwest and U S WEST already have discussed these matters in their Application. 21/ However, we will review the merger benefits of primary concern to the Commission here so that they are not lost due to the Opponents' failure to address them. 22/ Indeed, these benefits actually argue for expedited approval of this transaction under Sections 214 and 310. The sooner the merger closes, the sooner the benefits will start to flow to the public.

1. Faster Deployment of Advanced Services.

Merger Opponents first disregard the positive impact of the transaction on the provision of advanced services, both inside and outside the U S WEST region. This is a case of one plus one equaling far more than two. Each company holds broadband assets and expertise that complement those of the other. Together they will be better positioned to deploy those resources more rapidly, and

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21/ *See* Application at 14-18.

22/ These benefits also are described in more detail in the attached Carlton/Sider Declaration, Attachment A, at 8-10.

to become a regional, national and global leader in the provision of advanced services and technologies.

For its part, Qwest recently completed the construction of a state-of-the-art, nationwide, 18,500 mile OC-192 fiber optic, Internet protocol network. This network operates at speeds of up to 10 Gigabits per second and reaches 150 cities across the United States. The currently lit portion of the 48-fiber network has sufficient capacity today to handle all the traffic now carried by AT&T, MCI WorldCom, and Sprint combined. 23/ In addition, Qwest's network has unused capacity to permit the addition of ten times as many more fibers. Qwest has invested heavily in broadband international facilities, 24/ and its Internet and web hosting businesses also are global in scope.

U S WEST, in turn, has led the industry in its deployment of digital subscriber line (DSL) technology in the local loop, enabling subscribers – both residential and business – to maximize the speeds with which they transmit data and access the Internet. U S WEST already is providing DSL service in 40 in-region cities and serves about 40 percent of all DSL customers nationwide. U S WEST has well over 100,000 Internet access subscribers, and is offering them such

23/ *See* Backgrounder Fact Sheet – Next Generation Network www.qwest.com/press/qwest-uswest.html.

24/ Qwest's network extends 1,400 miles into Mexico, and includes undersea cables in the Atlantic Ocean. In addition, Qwest is part of a joint venture with KPN, the Dutch Telecommunications Company (KPNQwest), which is building an 18,100 mile European network that will connect 39 cities. Qwest also is part of a consortium that is building undersea fiber links to Japan and in the Asia Pacific Region.

advanced network-based vertical services as site-blocking, virus protection, and privacy measures. U S WEST also provides an innovative one-number PCS service, and through its Yellow Pages business is building an electronic commerce platform.

The merger recognizes the natural fit between these two companies. Qwest has a high speed national network but needs to offer customers broadband local connectivity to take full advantage of that asset. U S WEST is the market leader in DSL deployment. Post-merger, U S WEST's technical and market expertise immediately can be exported beyond the 14 state region, helping the combined company more rapidly offer broadband connectivity to the Qwest network.

Conversely, while U S WEST has DSL expertise, it does not own (even within its own region) a long-haul network that would enable it to provide the full range of advanced services to its customers. 25/ Once the combined company satisfies Section 271, it will be positioned to expand its in-region broadband service offerings much more rapidly using the springboard of the high speed Qwest network. 26/

In sum, the merger will benefit the public by enabling the combined company to deploy advanced services more quickly, more broadly, and more effectively than either company could standing alone. The merger will promote the

25/ Unlike many of the other RBOCs, U S WEST does not own, but rather leases, about 98 percent of its in-region interLATA facilities. These facilities today are used for official (internal) communications. It also does not own any interLATA long distance switches.

26/ As discussed below, the incentive to make early use of the Qwest network for in-region interLATA services constitutes a strong added incentive for U S WEST to satisfy Section 271's requirements. *See* Section I.C.3.b., *supra*.

Congressional goal, embodied in Section 706 of the 1996 Telecom Act, of accelerating the deployment of advanced services to all Americans. 27/ The beneficiaries will be consumers in the U S WEST territory and beyond.

2. Stronger Competition With Larger Firms Created by Other Mergers.

Merger Opponents also fail to credit a second public interest benefit of the transaction: stronger nationwide competition. The Commission already has approved -- or is being asked to approve -- other much larger telecommunications combinations, including (a) SBC-Pacific Telesis-SNET-Ameritech, (b) Bell Atlantic-NYNEX-GTE, (c) AT&T-Teleport-TCI-MediaOne, and (d) WorldCom-MCI-MFS-Brooks-Sprint. These huge combinations have significant horizontal elements that are entirely lacking in the Qwest-U S WEST merger. The public clearly will benefit from this merger insofar as it creates a stronger competitor to these giants. 28/

This merger, for example, will strengthen the resources and ability of the combined company to enter local markets outside the U S WEST region. The Commission recently approved the SBC-Ameritech merger, notwithstanding finding serious public interest concerns, in part because the FCC so valued SBC's commitment to enter the local market outside its territory. Indeed, the Commission established penalties if SBC does not follow through with this entry. 29/ Yet here

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27/ *See* 47 U.S.C. § 706.

28/ *See* Carlton/Sider Declaration, Attachment A, at 6-7, 9.

29/ *Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations from Ameritech Corp. to SBC Communications, Inc.,* CC Docket

Qwest *already* is active outside the U S WEST region, and its ability to draw on U S WEST local exchange expertise will simply accelerate that process.

More broadly, the Qwest-U S WEST merger will permit the combined company to compete more effectively for the "national/local customer" -- that is, the multi-location business customer that would prefer to buy all its communications services (including its local exchange services) from a single supplier. These are the customers that the FCC's conditions will encourage SBC to solicit in the U S WEST region and elsewhere, and that also will be the target of other merged ILECs with far more extensive local footprints. 30/ For example, the recently merged SBC-Ameritech will control approximately 33 percent of the customer lines served by the nation's largest ILECs. 31/ Post-merger, Bell Atlantic-

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No. 98-141, FCC 99-279 at ¶¶398-99 (released Oct. 6, 1999) ("SBC-Ameritech Order").

30/ *Id.; see also Application of GTE Corp., Transferor, and Bell Atlantic Corp., Transferee, for Consent to Transfer of Control*, CC Docket No. 98-184 (filed Oct. 2, 1998.)

31/ *Preliminary Statistics of Communications Common Carriers*, Report, 1998 WL 1058118, available at http://www.fcc.gov/Bureaus/Common_Carrier/Reports/FCC-State_Link/SOCC/98psocc.pdf, at p.3 (released May 28, 1999) ("*Statistics of Common Carriers*"). The FCC's "Statistics of Communications Common Carriers" compiles data from the country's largest incumbent local exchange carriers, which include all of the RBOCs, ALLTEL Corp., Citizens Utilities Co., Frontier Corp., GTE Corp., and Sprint Corp., and their various holding companies, if any.

GTE will serve approximately 37 percent of these customer lines. 32/ In comparison, U S WEST has only 9.5% of these lines. 33/

The combined company also will be better positioned to compete with AT&T, with its large long distance market share and its (current and proposed) control over a large percentage of the nation's cable television subscribers. If the MediaOne merger is approved, AT&T cable systems would pass approximately one-third of the nation's homes in addition to AT&T's exclusive arrangements with other operators. AT&T will have sole use of those local cable facilities to serve customers. The ability of AT&T to offer integrated packages of telephony, Internet, and video services presents a serious challenge to all its competitors, including the applicants here.

The Merger Opponents apparently hope the Commission will ignore the benefits to consumers of creating stronger competition to the new telecom giants. Qwest and U S WEST, however, are confident that the Commission will not be misled.

32/ *Id.*

33/ *Id.* As noted *supra*, these figures are based only on data from the nation's largest ILECs. However, if data from the remaining, smaller, local exchange carriers were also incorporated, these percentages of total customer lines would, at most, decrease only nominally. For example, the marginal effect of including all carriers, as opposed to only those reporting for *Statistics of Common Carriers*, can be seen in the example of SBC-Ameritech. *Compare*, *Id.* at 3 (reflecting SBC-Ameritech combined control of 33% of lines), *with SBC- Ameritech Order*, FCC 99-279, at ¶ 31 (reporting SBC-Ameritech combined control of 31.9% of nation's access lines).

3. Powerful New Incentives for U S WEST to Satisfy Section 271.

Finally, the Merger Opponents ignore, or simply dismiss out of hand, the applicants' observation that the merger will increase incentives for U S WEST to enter the interLATA market as soon as possible. 34/ Yet these incentives are a powerful additional reason for rapid Commission action here. This matter is discussed in more detail in the declaration of Bruce Owen of Economists, Inc., provided as Attachment B.

a. Incentives to eliminate out-of-region competitive disadvantages.

The first new incentive arises from the fact that, in divesting its in-region interLATA business, Qwest is taking on a significant competitive disadvantage compared with other national interexchange carriers. 35/ The post-merger company will have a doughnut-shaped footprint with a 14-state hole. Inside the hole the company will be unable to provide originating long distance, terminating 800, private line, and other prohibited interLATA services. 36/

As a consequence, Qwest will be seriously hampered in its ability to retain the out-of-region business of its existing customers, to compete for new customers out-of-region, and to grow its existing nationwide business. Multi-location business customers generally purchase interLATA services on a nationwide

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34/ *See, e.g.*, McLeod Comments at 28-32.

35/ *See* Owen Declaration, Attachment B, at 8, 10-12.

36/ *See generally* 47 U.S.C. § 271 (listing of prohibited and permitted interLATA services).

basis. They typically solicit nationwide service proposals and negotiate nationwide price discounts. They also generally prefer dealing with a single provider and having service provisioned over a single integrated network. 37/

The interLATA prohibition, then, will have two effects. First, Qwest will not be able to win all the customer business and revenues otherwise available to it. It will lose all its in-region interLATA business, and will suffer impacts in the out-of-region market from its inability to offer "one stop shopping" for interexchange service. Second, Qwest's marketing costs will increase, especially in the national account arena. Qwest will face special challenges trying to market stand-alone out-of-region services.

At the same time, Qwest's network costs will not be materially reduced by the divestiture of the "doughnut hole." Qwest still will have to maintain its nationwide network even though usage of that network will be constrained. 38/ The costs of that network are largely fixed or sunk. In addition, many costs related to network planning, operation, maintenance and management (the cost of the Network Operations Center, for example) do not vary with the capacity utilization

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37/ In the wholesale market, post-merger Qwest will be the only carrier's carrier with a nationwide network but without a nationwide offering.

38/ Qwest will continue to use network facilities in the U S WEST region for certain services permitted by Section 271, including delivery of long distance service originating out of region, and transmission of services that transit but do not originate or terminate in the region. However, Section 271 restrictions will constrain the usage of such facilities following divestiture and prior to Section 271 relief.

rate. 39/ The variable cost of using this in-place network to provide interLATA services is therefore very small, particularly when compared to the cost of leasing or building that network from scratch. 40/ Post-closing, the unit cost of using the Qwest network to provide service to out-of-region customers will increase because fixed costs now will be spread over less traffic.

Indeed, it is highly significant that no RBOC to date has engaged in major interexchange service activity outside its region, even though such activity is permitted by the Telecom Act. This fact itself demonstrates the serious disadvantages inherent in offering interexchange services in competition with AT&T, MCI WorldCom and Sprint without a national capability.

In sum, Qwest will face a significant opportunity cost for every month that it cannot use its valuable interLATA network to offer nationwide retail and wholesale products. 41/ Qwest and U S WEST are fully aware of that cost, and partly for that reason are committed to satisfy Section 271 on an accelerated basis.

39/ Such costs could vary, however, if new capacity is added and the geographic reach of the network is expanded.

40/ Once a fiber optic network is in place, the marginal cost of transmission over that network is quite low. *See, e.g.*, W.K. Viscusi, J. M. Versons, and J.E. Harrington, *Economics of Regulation and Antitrust, MIT, 1995*, at 496 ("[T]he investment of MCI and Sprint in their long-distance networks, whether microwave or fiber optics, is largely sunk so that the marginal cost of operation is relatively low."); *Telegeography 1999*, Telegeography Inc., 1998 at 20 ("The cost of routing calls is diminishing exponentially . * * * The per minute cost of carrying a voice call on [new trans-oceanic submarine] cables is miniscule.")

41/ *See* Owen Declaration, Attachment B, at 10-12.

b. Incentives to make full use of the Qwest network asset.

As discussed in the Owen Declaration, the post-merger company also will have additional incentives to satisfy Section 271 because the company now already will own an interLATA network. 42/ This fact is highly significant. U S WEST has no such network today, either in-region or out-of-region. 43/ But post-merger the combined company already will have incurred most of the costs of providing interLATA service because it already will own the interLATA facilities.

This fact has important consequences. First, it means that the merged company will be able to enter the interLATA market immediately upon Section 271 relief, with its own high capacity state of the art interLATA network. It will not incur the time and cost involved in constructing a facilities network on its own, nor will it have to depend on reselling the services of another carrier. 44/

Second, and more important, the low variable cost of using the existing Qwest interLATA network will make provision of in-region interLATA services more profitable for the combined company than it would be for U S WEST alone. The merger therefore will create a stronger incentive to satisfy the Section 271 requirements. Expeditious Section 271 approval will allow the combined company

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42/ Owen Declaration, Attachment B, at 12.

43/ As noted above, U S WEST leases about 98 percent of the interLATA facilities it uses today to provide official services in its region, unlike many other RBOCs.

44/ Owen Declaration, Attachment B, at 9-10.